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C O N F I D E N T I A L SECTION 01 OF 03 CARACAS 002128

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ENERGY FOR CDAY AND ALOCKWOOD
NSC FOR JCARDENAS AND JSHRIER

E.O. 12958: DECL: 10/02/2017
TAGS: EPET ENRG EINV ECON ELAB VE
SUBJECT: PETROCEDINO'S COMPLICATED BIRTH

REF: A. CARACAS 1822
¶B. CARACAS 1655

Classified By: Economic Counselor Andrew N. Bowen for Reason 1.4 (D)

¶1. (C) SUMMARY: The creation of Petrocedino, the joint venture formed from the former Sincor strategic association, poses a variety of challenges for its private sector participants. The new company will extract and upgrade extra-heavy crude oil in the Faja region. Venezuelan state oil company PDVSA will hold a 60% stake, French oil company Total a 30.323% stake, and Norwegian oil company Statoil a 9.677% stake in the company. On the plus side, the joint venture's president is competent and private sector partners control key operational posts. The joint venture has begun offering employment packages to its employees that are substantially below the Sincor compensation packages. Labor continues to disrupt operations and human resources has become politicized. END SUMMARY

THE BIRTH OF PETROCEDINO

¶2. (SBU) The Official Gazette published the agreement that forms Petrocedino, the joint venture created from the former Sincor strategic association, on October 29. Under the terms of the agreement, PDVSA will hold a 60% stake, Total a 30.323% stake, and Statoil a 9.677% stake in the company. The company is legally entitled to carry out exploration, extraction, transport, and storage of crude oil as well as refining/upgrading activities in a 399.25 square kilometer block. (COMMENT: As noted in Reftel A, the size of Petrocedino's block is larger than the original Sincor block despite repeated BRV statements that block sizes would be reduced. END COMMENT). The joint venture is also empowered to enter into contracts for petroleum services but is barred from assigning the operator function to another entity.

¶3. (SBU) Under the terms of the contract, Petrocedino has

the right to market its upgraded crude oil and products at international market prices to non-related parties. However, it must sell all crude oil that it produces above its current upgrading capacity to PDVSA as well as all other natural hydrocarbons that it extracts and does not utilize in its operations with the exception of crude oil upgraded in third party facilities or crude used for royalty payments. Petrocedino is authorized to receive payment for crude and products in U.S. dollars and to hold bank accounts outside of Venezuela that can be utilized for operations.

¶4. (SBU) Petrocedino is subject to a royalty rate of 30% and an income tax rate of 50%. In addition, it must pay a science tax and devote 1% of pre-tax profits to a social development program. The joint venture is also subject to an extraordinary tax that is equal to the difference between half the value of the crude oil extracted before upgrading and other natural hydrocarbons extracted from the block and the sum of payment for royalties, the extraction tax, income taxes, the science tax, social spending, and any other tax based on income.

STATOIL'S TAKE ON THE NEW JOINT VENTURE

¶5. (C) Petrocedino/Sincor Deputy General Manager Jane Nagy (strictly protect throughout) told Petroleum Attache (Petatt) on November 1 that there are real problems in getting the Petrocedino joint venture off the ground but that the contract was not one of them. She indicated that Statoil is pleased with the contract, particularly the provisions dealing with marketing and governance (Reftel A). In

addition, Statoil was able to place its personnel in the key positions of marketing, finance, information technology, and contracting/procurement. Nagy stated Total, on the other hand, was angry that Statoil was able to secure so many key positions despite the fact that it has the smallest equity stake in Petrocedino. Nagy attributed Statoil's success in part to its excellent working relationship with CVP president Eulogio Del Pino. Nagy later stated that PDVSA controls the auditing department and noted that PDVSA officials had little idea of what an audit entails.

¶6. (C) Nagy stated Statoil is also pleased with Petrocedino president Manuel Alvarez, a PDVSA secondee. She noted Alvarez was competent and fully understood what it takes to run Petrocedino. Nevertheless, she expressed concern that Alvarez would not hold his post for long due to poor health, family problems, and PDVSA's tendency to constantly shift senior managers from one post to another. Nagy explained that Alvarez has had a stroke and his son has cancer.

LABOR CONTINUES TO BE A MAJOR HEADACHE

¶7. (C) Despite the generally favorable terms of the contract, Petrocedino faces a number of operating challenges, primarily in the area of human resources. The joint venture recently began offering employees their new employment package, which contains a significantly lower salary than the Sincor package. Nagy stated the package is not as bad as some employees claim since roughly 20% of the salary was shifted to benefits. She admitted that some employees, however, would face a significant cut in salary. To date, Petrocedino has only offered the new package to 29 employees. Nagy stated rumors are circulating that 200 employees quit the former Ameriven strategic association after receiving their new employment packages. (NOTE: PDVSA (30%), ConocoPhillips (40%), and Chevron (30%) were originally the shareholders in the Ameriven strategic association. Following the departure of ConocoPhillips, PDVSA assumed its equity stake and the strategic association became the Petropiar joint venture. The agreement forming Petropiar

appeared in the same Official Gazette as the Petrocedino agreement. END NOTE)

¶8. (C) Nagy also complained that labor unions continue to cause problems at Petrocedino. As noted in Reftel B, union members had blocked the road to the upgrader 33 days between January and August. When asked if protests were continuing, Nagy replied that between August and November the protesters had blocked the road an additional 10 to 15 days.

¶9. (C) Nagy also stated that Petrocedino officials had difficulty disciplining employees due to the politicized nature of the human resources department, which is run by a PDVSA secondee, as well as the power of the labor unions. She stated Petrocedino officials were pushing PDVSA to remove the current human resources director because he has been basing employment decisions on his personal vendettas against various employees as well as his political beliefs. She added that Petrocedino had already replaced one human resources director because he was driving out employees on the basis of their political beliefs. Nagy claimed that CVP president Del Pino understood that Petrocedino could not afford to fire large numbers of employees for political reasons but added that that message had not reached Petrocedino human resources officials. She expressed concern that Petrocedino would not be able to maintain production levels.

¶10. (C) Nagy stated labor unions continue to hold massive

amounts of power at Petrocedino. She stated some employees regularly carry firearms and only retain their jobs due to union connections. In a recent case, a female cleaner threatened a Petrocedino employee and then sent union thugs to threaten him. When Nagy complained to the human resources department, they failed to respond. She later saw a memo from the head of human resources stating that no disciplinary action would be taken because the cleaner was "one of our people."

¶11. (C) Nagy stated safety is her primary concern and that she would not hesitate to halt operations if she felt they could not be carried out safely. She added that PDVSA officials have parroted her language on safety but it remains to be seen if they would actually halt operations if their superiors told them to continue operations at all costs. Nagy also complained that Statoil officials were pressuring her to continue maintaining Statoil's high safety standards within Petrocedino but were oblivious to the politicized operating environment within the joint venture.

CONCERNS OVER MAINTENANCE SHUTDOWN

¶12. (C) Nagy stated she still has serious concerns over the major maintenance shutdown scheduled for February (Reftel B). Although the shutdown will occur in only three months time, PDVSA has not been able to provide details on its ability to provide Mesa 30 crude to blend with the extra heavy crude that Petrocedino produces. If PDVSA is unable to provide the lighter crude for blending purposes, Petrocedino would have to halt extraction operations since it cannot market the extra heavy crude by itself. Nagy stated Petrocedino would need 55,000 barrels of Mesa 30 per day in order to continue production.

COMMENT

¶13. (C) Nagy's comments regarding Petrocedino's operations and structure and the text of the contract are in line with previous reporting in Reftels A and B. We were surprised, however, by her comments regarding the continuing power of labor unions in the Faja. A number of Embassy sources have told us that the BRV has completely broken the power of the

unions. When Petatt noted the widespread perception that the recently signed collective bargaining agreement failed to deliver significant benefits to organized labor, Nagy replied that this was due to the fact that the BRV had bought off labor leaders and was not a true indication of the strength of the leaders.

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